PREPARED DIRECT TESTIMONY OF
NICHOLAS T. SHEA
ON BEHALF OF
CENTRAL ILLINOIS LIGHT COMPANY
DOCKET NOS. 00-0815 and 00-0816

Q1: Please state your name and business address.

A1: My name is Nicholas T. Shea, and my business address is 300 Liberty Street, Peoria, Illinois 61602.

Q2: By whom are you employed and in what capacity?

A2: I am employed by Central Illinois Light Company (CILCO or Company) as the Director of Rates and Regulatory Affairs.

Q3: Please briefly describe your educational background and work experience.

A3: I am a graduate of Western Illinois University, with a Bachelor of Science degree and a Masters of Business Administration degree. I began my employment with CILCO in the accounting unit in 1972, and held several management positions within that area. Thereafter, I held positions in the Financial, Human Resources, Internal Audit, Information Technology, and Fuel Supply areas of the Company. I entered my current position in late 1995.

Q4: Please describe your duties in your present position.

A4: I am responsible for the development of rates, terms, conditions and programs for the provision of public utility service, and for ensuring their implementation. My duties involve the evaluation of the impact of regulatory issues on CILCO, and the development and

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Q4: Please describe your duties in your present position.

A4: I am responsible for the development of rates, terms, conditions and programs for the provision of public utility service, and for ensuring their implementation. My duties involve the evaluation of the impact of regulatory issues on CILCO, and the development and advocacy of CILCO's position in regulatory proceedings. I have responsibility for implementing the rules and regulations of the Illinois Commerce Commission (Commission) applicable to the Company, and for assuring compliance by the Company with regulatory requirements.

Q5: What is the purpose of your testimony in this proceeding?

A5: In Docket No. 00-0815, I will address the issues set forth in Sections 7-101, 7-102 and 9-201 of the Public Utilities Act (Act), on which the Commission must make findings prior to approving the execution and performance of agreements between CILCO and its affiliate, AES Medina Valley Cogen, L.L.C. (AES Medina), to the extent required by Illinois law. I will also address the exclusion from CILCO's automatic adjustment clauses of the costs and revenues related to gas and other support services provided by CILCO to AES Medina. In Docket No. 00-0816, I will address the issues set forth in Section 79z-5a(k)(2) of the Public Utility Holding Company Act of 1935, as amended (PUHCA), on which the Commission must make findings concerning CILCO's purchase of energy at wholesale from AES Medina, an affiliate that is requesting certification from the Federal Energy Regulatory Commission (FERC) as an Exempt Wholesale Generator (EWG).

Q6: Please describe the proceedings now pending at the FERC which concern the proposed transactions between CILCO and AES Medina.

A6: AES Medina has filed the Tolling Agreement, CILCO Exhibit 1.1, with FERC in Docket No. ER01-788-000. AES Medina has requested FERC to certify it as an EWG in Docket No. EG01-83-000. CILCO has filed an Interconnection Agreement with AES Medina in Docket

No. ER01-769-000.

Q7: Please describe the approval being requested from FERC applicable to the Tolling Agreement, and the approval being requested from the Commission.

A7: The Tolling Agreement, CILCO Exhibit 1.1, is AES Medina's FERC rate schedule and service agreement for wholesale electric sales being made by AES Medina to CILCO. AES Medina is asking FERC to approve the rates for Energy Payments, specified in Exhibit G of the Tolling Agreement, and terms of the energy sales under Section 205 of the Federal Power Act. Because AES Medina and CILCO are affiliates, the terms of this sale will be reviewed by FERC using the criteria it has developed in similar previous cases. The power and energy to be provided to CILCO under the Tolling Agreement will be provided at wholesale in interstate commerce, and I have been advised that the rates, terms and conditions of the Tolling Agreement applicable to the power and energy fall under the jurisdiction of the FERC. However, because of the affiliate relationship between CILCO and AES Medina, CILCO's purchase of steam heat service and chilled water service, based on the payments specified in Exhibit G of the Tolling Agreement, and other provisions of the Tolling Agreement that relate to the purchase and sale of steam heat and chilled water service are within the jurisdiction of the Commission under the provisions of Section 7-101 of the Act, relating to transactions between public utilities and their affiliates. Therefore, to the extent subject to Commission jurisdiction, CILCO is requesting Commission approval for CILCO to enter into and perform the Tolling Agreement.

Q8: Please describe the certification being requested from FERC by AES Medina applicable to its status as an EWG.

A8: Pursuant to the criteria in Section 79z-5a(k)(2) of PUHCA, FERC has issued regulations in Section 365 which outline the requirements for certification as an EWG. AES Medina has asked FERC to certify that it qualifies as an EWG.

Q9: Please describe the approval of the Interconnection Agreement being requested by CILCO from FERC.

A9: Under Section 205 of the Federal Power Act, and FERC's requirements applicable to Open Access Transmission Tariffs (OATTs), the FERC considers an Interconnection Agreement to be a service agreement under CILCO's OATT. The Interconnection Agreement between CILCO and AES Medina is similar to the Interconnection Agreement that CILCO recently had approved by FERC with another co-generator, BioEnergy. The Interconnection Agreement outlines the terms under which AES Medina will operate in relation to the requirements of CILCO's transmission system and the security coordinator that will be overseeing those operations. The Interconnection Agreement also provides for the rates charged AES Medina by CILCO for metering and other services such as telecommunications, applicable to the delivery of the energy generated by AES Medina into CILCO's system. I have been advised that FERC has jurisdiction over the terms, conditions and rates for this interconnection service.

Q10: Section 7-102 of the Act and PUHCA require the Commission to determine whether the public will be convenienced by the transactions proposed by CILCO and AES Medina. Are these transactions in the public interest?

A10: As Mr. Haynes points out in his testimony, the construction of a new, natural gas-fueled cogeneration facility to replace Caterpillar's existing coal-fired steam plant is strongly in the public interest. CILCO is currently capacity-deficient, in that CILCO must purchase power and energy from third-party providers to meet the on-peak requirements of CILCO's bundled electric customers. The cost of such purchased power and energy is generally higher than the cost of generation from CILCO's own generating units, and the increased cost is passed on to CILCO's customers through CILCO's fuel adjustment clause. The execution and performance of the Tolling Agreement will reduce by approximately 40 Mw the load placed upon CILCO's system by Caterpillar's Mossville, Illinois Performance Engine Products Division (PEPD) plant, and Mapleton Foundry, and thereby reduce in an equal amount CILCO's dependence upon the energy market to provide power and energy for CILCO's remaining bundled customers. This should result in reduced overall energy costs to the bundled customers. A new electric generating plant will directly benefit CILCO's bundled electric customers by reducing the amount of higher-cost energy CILCO is required to purchase from third parties to meet native load requirements. The new plant will also benefit all customers in Illinois with the addition of 40 Mw of cleaner and more efficient generation that will help Illinois to avoid some of the electric supply problems plaguing California. Not only will overall energy costs be reduced, there will also be a reduction in the price volatility to which bundled electric customers are exposed when purchases of power and energy are made at market-based prices. During any periods when the total power and energy produced by Medina are not used by Caterpillar, the excess energy may be used by CILCO to serve its bundled customers. In addition, if the Medina facility is placed into service, Caterpillar will make available to CILCO through displacement of energy, at no cost to CILCO other than the cost of operation and maintenance, 14 Mw of capacity from generating sets located in the Caterpillar plants. These generating units were previously used by Caterpillar during interruptible periods pursuant to an interruptible service contract with CILCO. CILCO now will be permitted to use the capacity during other periods, including periods when the cost of operating the generating sets is less than the cost of alternative power and energy. The reduced cost will directly benefit CILCO's customers.

Q11: What are the rate impacts on CILCO's bundled retail customers of the proposed transactions between CILCO and AES Medina?

A11: CILCO will be required to pay a demand charge to AES Medina that will not be directly recovered through the resale of power and energy produced by AES Medina. However, except in special circumstances which are not likely to occur, CILCO's base rates cannot be increased until the end of the mandatory transition period on January 1, 2005. Therefore, CILCO's bundled customers will not experience any increase in base rates before January 1, 2005, and any increase after that time is subject to a rate proceeding filed by CILCO with this Commission. As a result of the execution and performance of the Tolling Agreement, CILCO's retail customers will obtain a substantial reduction in fuel adjustment charges and in exposure to market risk. Even if CILCO's fuel adjustment clause is eliminated pursuant to a petition presently pending before the Commission in Docket No. 00-0579, savings to bundled customers as a result of the Tolling Agreement have been included in the calculation of the FAC charges to be included in base rates when the FAC is eliminated. Therefore, there are multiple direct benefits to CILCO's customers as a result of purchasing wholesale energy from AES Medina pursuant to the Tolling Agreement. However, without the determinations requested in Docket No. 00-0816, CILCO cannot lawfully purchase wholesale energy from AES Medina.

Q12: What authority is CILCO requesting under Section 9-201 of the Act?

A12: CILCO is also requesting Commission approval under Section 9-201 of the Act, to the extent required by law, not to include in CILCO's automatic adjustment clauses any costs and revenues related to gas and other services provided to AES Medina's facility to produce electric energy, steam heat service and chilled water service resold to Caterpillar, and any costs and revenues related to energy, steam heat and chilled water service received from Medina and resold to Caterpillar. Most of the power and energy, and all the steam heat service and chilled water service will be resold by CILCO to Caterpillar under a competitive services agreement authorized by Sections 16-102 and 16-116(b) of the Act. As I noted above, any power and energy available from the cogeneration facility that is not sold to

Caterpillar as a competitive service will be used by CILCO to provide power and energy to CILCO's other customers, and CILCO requests authorization to include the costs and revenues related thereto in its fuel adjustment clause.

Q13: What is the status of AES Medina under PUHCA?

A13: It is a condition of the Tolling Agreement that AES Medina be an Exempt Wholesale Generator (EWG) under the provisions of the PUHCA. AES Medina meets the requirements of PUHCA to be an Exempt Wholesale Generator because AES Medina will operate only the cogeneration plant and will sell the electric power and energy output of the cogeneration plant solely at wholesale, and as I described above, AES Medina has an application at FERC pending to certify its status as an EWG.

Q14: Does PUHCA require any additional approval of the transactions between AES Medina and CILCO?

A14: Yes. Section 79z-5a(k) of PUHCA provides that after October 24, 1992, an electric utility company like CILCO may not enter into a contract to purchase electric energy at wholesale from an EWG if the EWG is an affiliate or associate company of the electric utility unless, prior to the electric utility entering into the contract, every State commission having jurisdiction over the retail prices of the electric utility makes each of the following specific determinations:

> (i) A determination that such commission has sufficient regulatory authority, resources and access to books and records of the electric utility company and any relevant associate, affiliate or subsidiary company to exercise its duties under this subparagraph.

(ii) A determination that the transaction —

I. will benefit customers,

II. does not violate any State law (including where applicable, least cost planning),

III. would not provide the exempt wholesale generator any unfair competitive advantage by virtue of its affiliation or association with the electric utility company, and

IV. is in the public interest.

Q15: Does the Commission have sufficient regulatory authority over CILCO and sufficient access to the books and records of AES Medina related to transactions with CILCO to assure that the other determinations requested of the Commission in this case are and will remain accurate?

A16: Yes. Because CILCO is an electric utility doing business in Illinois, the Commission has regulatory jurisdiction over CILCO, including the annual review of the prudence of CILCO's actions with respect to costs recovered through the fuel adjustment clause, and the right to require information from CILCO with respect to regulated transactions and transactions with affiliates. The Commission has in place rules which govern the conduct of public utilities with their affiliates, including a requirement for biennial audits by utilities of their transactions with affiliates. The Commission has also approved specific procedures applicable to CILCO in dealings between CILCO and its affiliates.

Q17: What guidelines and procedures are currently in place at CILCO with respect to transactions with its affiliates?

A17: CILCO has on file with the Commission guidelines and procedures covering transactions between CILCO and its affiliates. These guidelines were adopted and filed pursuant to the Commission's Order in Docket No. 84-0413. In addition, CILCO has filed guidelines and procedures with the Commission applicable to all non-utility activities of CILCO. These guidelines were adopted pursuant to the rule recently approved by the Commission at 83 Ill. Adm. Code, Part 416, *Accounting for Non-Public Utility Business of Electric Utilities*. Both sets of procedures assure that there will be no subsidization of affiliate or other non-utility transactions. CILCO is also required by the Commission's rules to make biennial audits of its compliance with these procedures. CILCO recently completed those audits and filed them with the Commission on November 30, 2000. The audit reports found that CILCO was in compliance with the guidelines covering affiliate and other non-utility transactions. These audits will be performed at two year intervals in the future, and provide continuing assurance that there will be no subsidy of non-utility activities by CILCO or its customers.

Q18: Does Section 7-101 of the Public Utilities Act give the Commission jurisdiction over affiliated interests like AES Medina having transactions with public utilities like CILCO under the Commission's jurisdiction, to the extent of access to all accounts and records of such affiliated interests relating to such transactions?

A18: Yes, as the Commission has found in prior proceedings, such as its approval of the merger of AES Corporation with CILCORP Inc. in Docket No. 98-0882, Section 7-101 provides the Commission with broad authority over affiliate transactions such as the ones proposed between CILCO and AES Medina, including access to accounts and records of joint or general expenses, any portions of which may be applicable to such transactions, and the authority to require such reports as the Commission may prescribe with respect to such transactions to be submitted by such affiliated interests. These provisions, together with the Commission's regulatory jurisdiction over CILCO, assure that the Commission will be able to review and enforce the other determinations requested in this proceeding and required by PUHCA to permit CILCO to purchase wholesale energy from an associate company that is an EWG.

Q19: Does the execution and performance of the Tolling Agreement violate any Illinois law?

A19: No. Section 8-403 of the Public Utilities Act encourages the economic use of cogeneration. Further, Section 16-111(g)(3) of the Public Utilities Act specifically contemplates that electric utilities in Illinois will purchase wholesale power and energy from affiliated entities pursuant to prices, terms and conditions approved or allowed into effect by the FERC. As I noted above, the Tolling Agreement between CILCO and AES Medina is subject to FERC approval, and the prices, terms and conditions of the sale of power and energy to CILCO by AES Medina under the Tolling Agreement will be approved by FERC. Accordingly, the execution of the Tolling Agreement and the sale of wholesale energy by AES Medina to CILCO will not violate Illinois law.

Q20: Will the purchase of wholesale energy by CILCO from AES Medina provide AES Medina with any unfair competitive advantage?

A20: No. The prices, terms and conditions of the sale of wholesale energy by AES Medina will be subject to approval by FERC. Moreover, the amounts paid by CILCO to AES Medina for energy, steam heat service, and chilled water service will, except for the payment of fixed energy charges, be essentially a pass-through to Caterpillar. As an interested third party whose economic interest will be directly affected by any advantage given to AES Medina, Caterpillar will monitor all operations and transactions to protect its rights. Because the prices, terms and conditions must be approved by FERC and Caterpillar will be protecting its own interests, the purchase of wholesale energy under the Tolling Agreement will not result in any unfair advantage to AES Medina. As I stated above, under Section 7-101 of the Public Utilities Act, the Commission will have continuing oversight over the books and records of both CILCO and Medina with respect to transactions between them. The Commission will also have access to biennial audits of transactions between CILCO and its affiliates. These provisions further assure that there will be no unfair advantage to AES Medina.

Q21: Paragraph (3) of Section 7-204(b) requires the Commission to determine that costs and facilities will be fairly and reasonable allocated between utility and non-utility activities in such a manner that the Commission may identify those costs and facilities which are properly included by the utility for ratemaking purposes. How is this requirement satisfied?

A21: The guidelines and procedures I previously described, together with the biennial audits required by Commission rules to determine compliance with those guidelines and procedures, provide assurance that the costs and facilities with respect to non-utility transactions will be fairly and reasonably allocated to non-utility activities. The procedures applicable under 83 Ill. Adm. Code, Part 506, require that all non-utility transactions be recorded in sub-accounts. This makes it easier for the Commission as well as CILCO's own auditors to review CILCO's non-utility activities to assure there is proper allocation of costs and facilities for ratemaking purposes.

Q22: How will the project's fuel costs be allocated between competitive and regulated electric production?

A22: In general, the project's fuel costs will flow through directly to Caterpillar. There will be times, however, when Medina's electric production is greater than Caterpillar's usage as a result of meeting Caterpillar's demand for steam heat. At those times, the excess power will be sold to CILCO retail customers other than Caterpillar. The cost of fuel used to generate the excess power will be included in the fuel adjustment charge calculation according to the following allocation formula:

$A - B = C$

A = The kilowatt-hours produced by Medina

B = The kilowatt-hours produced at Medina and sold to Caterpillar

C = The kilowatt-hours sold to CILCO retail customers other than Caterpillar

D x 6800 Btu/hour x C = E

D =Average Monthly cost of gas per Btu used at Medina

6800 Btu/kWh = The electric heat rate of Medina

E = Fuel cost of kWh sold to other CILCO retail customers

As a result of the ICC order specific to CILCO's 1999 FAC (Docket #99-0468), there is no distinction or benefit to retail customers outside or behind the CILCO system.

Q23: Can you provide an example, in those cases where CILCO would be selling kilowatt-hours from Medina to retail customers other than Caterpillar, what the impact to those customers would be?

A23: Here is a brief example of how the fuel costs would be captured in CILCO's FAC calculation.

Delivered Cost of Natural Gas	$3.00	$4.00	$5.00	$6.00
Heat Rate Btu/Kwh	6800	6800	6800	6800
Kwhs/MMBtu	147.06	147.06	147.06	147.06
Fuel Cost $/Mwh	$20.40	$ 27.20	$34.00	$40.80

The assumptions used are: 1cf = 1,000 Btu = 1 therm

1 ccf = 100cf = 100,000 Btu = 1 therm

1 mcf = 1,000 cf = 1.000,000 Btu = 10 therms

1 MMcf = 1,000 Mcf

1 Bcf = 1,000,000 Mcf

Assume 1 cubic foot of gas contains 1,000 Btu

Assume the price is 30 cents per therm or $3 per Mcf

Btu per Mcf / heat rate per Kwh = Kwh per Mcf or 1,000,000 / 6,800 = 147.06

Price per Mcf / Kwh per Mcf = cost per Kwh or 3 / 147.06 = $0.0204 per Kwh or $20.40/ Mwh

Q24: In requesting approval from the Commission for CILCO to exclude from the FAC the costs incurred and the revenues received for electricity provided to Caterpillar from the Medina facility, is CILCO requesting authorization to handle the FAC costs differently than was determined in Docket No. 99-0486?

A24: Yes. As I understand the Commission's decision in Docket No. 99-0468, all the energy costs of purchased power must be included in the FAC costs. CILCO is not permitted to dedicate or target purchased power for particular customers or groups of customers. In determining the FAC costs allocated to sales not subject to the FAC (CNS), including competitive sales, the average of the generation and purchased power costs is to be used. The exception is interchange sales, for which incremental costs are used. However, as a cogenerator, the Medina facility is a special case. The facility will provide electricity principally to its cogeneration host, Caterpillar, and Caterpillar will directly reimburse CILCO for the cost of gas used to generate electricity, steam heat service and chilled water service. Caterpillar will also provide make-up water and condensate to the facility. Under such circumstances, it is not reasonable or appropriate to include in the FAC costs which are to be reimbursed directly by Caterpillar. If the costs are included in the FAC, they could be double-recovered when Caterpillar pays all the costs and FAC customers are also allocated a portion of the cost.

Q25: When will electricity produced by the Medina facility be used for FAC customers?

A25: It is my understanding that other than during the initial testing period from March through June, 2001, when all the electricity will be used by CILCO, this will happen only when the facility is needed to produce steam heat service and Caterpillar does not require all the electricity produced in conjunction with the steam heat. In those cases, the costs of the electricity, calculated pursuant to a formula, will be included in the FAC just like other purchased power costs. However, the amounts of electricity from the facility that will be used for system sales will be relatively minor. Caterpillar will require most of the electricity to operate its PEPD facility.

Q26: Will there be occasions when the cost of electricity from the Medina facility will be higher than the incremental cost of alternative energy available to CILCO?

A26: Yes, that may be the case.

Q27: Does inclusion of such costs in the FAC violate the requirements of economic dispatch?

A27: No, it does not. In order for the cogeneration project to be viable, CILCO must be willing to accept the electricity produced as a by-product of steam heat service. The benefits of the project produce savings to customers that far exceed any temporary increase in the cost of purchased power. Because the overall charges to customers through the FAC will decline as a result of the project, the overall result represents economic dispatch.

Q28: Does the use of this methodology benefit CILCO's retail customers who pay FAC charges?

A28: Yes, CILCO believes this methodology benefits CILCO's retail customers who pay FAC charges. The biggest benefit of this project to CILCO bundled FAC customers is the increased availability of CILCO's coal-fired generation assets as a result of Medina generation being targeted to Caterpillar. If the purchase of energy from Medina by CILCO and delivered to Caterpillar must follow the 1999 order, gas-fired generation (which is currently at a premium to coal-fired generation) would be allocated to the bundled FAC customers 100% of the time. In effect, those customers would then be subsidizing Caterpillar. Under the methodology proposed in my testimony, the gas-fired generation at Medina would be allocated to CILCO's bundled FAC customers only when that generation is used to supply their load. There would be no Caterpillar subsidy.

Q29: Does this complete your prepared direct testimony?

A29: Yes, it does.